

Takeaways from CREFC Miami

Two Types of Specialty CMBS Assets That Carry Special Risks

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Morningstar Perspective

The prolonged decline of retail remains part of the conversation in commercial real estate, but CREFC's Wednesday panel on credit performance highlighted two assets that, even though they may not dominate headlines, present real concerns for investors. Student-housing properties and limited-service hotels usually don't represent a significant part of a CMBS deal's portfolio. Still, they can have just as extreme an outcome as troubled regional malls, according to the panelists.

Prime Finance's Luke Dann found that multifamily housing represents almost 18% by balance of his firm's specially serviced loans. Of those properties, 11 are student housing. "There's obviously the micro and macro dynamics in student housing, but it's a very specialized asset type," he said, "If something goes wrong, it can go really wrong." The leasing is very seasonal and follows the academic calendar, and the property's distance from campus is a key selling point for students. Dann estimates that the 11 student housing loans represent \$264 million, and he views all of them as problem loans.

Limited-service hotels could present the "death by a thousand cuts" dilemma, said David Harrison, senior vice president at Midland Loan Services. The largest concentration of limited-service hotels he's seen was in a 2013 deal that had 6.3% by balance. Dann added that his company has 39 loans backed by limited-service hotels in special servicing, under \$15 million in balance. In his opinion, they don't destroy a deal, but having them isn't a positive. In his experience, new supply to the market is nine times out of 10 an obstacle for hotels. Harrison noted that investors shouldn't be fooled by small loan sizes. Working out a troubled loan on a portfolio of limited-service hotels isn't less intensive than working out a large loan on a full-service hotel. He finds that the operators and owners of these types of hotels present a lot of challenges.

Investors should be aware of the distinct risks student housing and limited-service hotels present to their portfolios. Per the panelists, they may be small in size, but they can present problems, especially when things start to go awry.

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